



Investment Insights

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Six Steps to Financial Freedom

Often when we discuss investment planning with clients, the selection of investment vehicles is towards the bottom of the agenda. When it comes to achieving your financial freedom, there are many steps you can take that are within your control, steps that may have a far greater impact on your ability to reach your financial goals than selecting top-performing investments. Much attention is paid to predicting what the stock market will do in the coming year, or whether real estate is a good investment right now, but below are six important steps you can take now that will have a predictable and clear-cut effect on your financial picture.

Step One: Pay off all of your revolving credit balances

If you are carrying any credit card or installment debt (other than your mortgage), you should first pay that off entirely before starting an investment plan. Investing money that may earn 6% or 7% while you are paying 12% interest on a credit card just doesn't make financial sense. Get the bills taken care of first.

Step Two: Build a "rainy-day" fund

It is important for all households to have some cash reserves, held in a safe, liquid place like a money market account. By having a rainy-day fund, you can avoid having to tap into longer-term investment accounts should an unforeseen emergency arise. The amount of money one should hold in such an account varies by the stability of their financial situation. For example, if your employment is not secure, as is common in this difficult economy, you may want to err on the side of caution and hold more cash than usual in a rainy-day fund. The general rule of thumb is three to six months of living expenses, and until this amount has been set aside, you should hold back from making more ambitious, longer-term investments.

Step Three: Fund your retirement

Unless you are already retired, you share the goal of millions of other Americans of dreaming of a secure, enjoyable retirement. The best way to reach this goal is by saving money in a retirement plan. If your company offers a retirement plan (i.e. 401(k), Simple IRA, etc), make regular, ongoing contributions to it. Not only will the money grow tax-deferred until you withdraw it, you'll also get an immediate write-off for your contributions. In many cases, companies will also match your contribution to some extent, making this even more attractive. If you don't have access to a company-sponsored plan, consider establishing an IRA or ROTH IRA. Among our retired clients, we find their retirement accounts to be among their biggest assets. There are many retirement calculators available to figure out how much you should be contributing to reach your goals: www.bankrate.com has some nice ones to get you started.

Step Four: Fund your children's college education

It is common knowledge that the cost of a college education is soaring, and many studies have shown how important getting a college education can be towards finding good employment. The entire issue is tough for many parents to stomach, but this is clearly an area in which the earlier you start, the easier it is to tackle. There are many ways to save for college, but we've found that the tax advantages and structure of 529 College Savings Plans make them ideal in most situations. Again using financial calculators, it is easy to project the future cost of your child's college education, and working backwards from there you can figure out what amounts you will need to save to meet those future obligations. Set up a systematic monthly contribution to the account, start with an amount that is within your reach (many plans will let you invest as little as \$25 per month systematically), and bump your contributions up as you are financially able.

Step Five: Save for shorter-term goals

Once you've taken care of working towards fulfilling your retirement and paying for your child's education, you can start to save for other goals. This may include buying a vacation home, traveling, or just striving for more financial flexibility in the future. Although it is tempting to start with this step because shorter-term goals offer more immediate satisfaction, you can enjoy reaching these goals much more if you know that you have taken care of the longer-term goals first.

Step Six: Automate your plan

If you've made it this far, congratulations! You are in better financial shape than many, and you are now in control of your destiny. The final step is to automate your plan by setting up systematic contributions to all of your investment accounts. You can do this by having your financial advisor set up monthly deductions from your checking account to fund all of the various investment accounts you have. This is important because procrastination and lack of follow-through can kill even the best-laid financial plans. We like to think of this step as "paying yourself first". Before you start writing checks to the cable company, the phone company, or any of the myriad places your money goes each month, make sure you pay yourself first by having these monies go to your accounts. Once you've done this, you can spend the rest of your paycheck as you see fit without guilt and remorse because you have taken care of the most important obligation first: your obligation to yourself and your family.

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